United Nations E/2006/18

Economic and Social Council

Distr.: General
25 April 2006

Original: English

Substantive session of 2006
Geneva, 3-28 July 2006
Item 10 of the provisional agenda*
Regional cooperation

Summary of the economic and social survey of Asia and the Pacific, 2006

Summary

According to the *Economic and Social Survey of Asia and the Pacific 2006*, global economic growth slowed to 3.2 per cent in 2005, down from the record growth rate of 4.0 per cent in 2004. The growth rate of developing countries in Asia and the Pacific also decelerated moderately in 2005. The slowdown in the global economy and in developing countries in the Economic and Social Commission for Asia and the Pacific region was the result primarily of high and volatile oil prices and a softening of global trade. More expensive oil also heightened inflation in the region; however, overall price pressures remained mild by historical standards.

Prospects for 2006 indicate that gross domestic product growth should maintain its current momentum while price pressures should abate slightly. This is based on the following assumptions: oil prices will not increase significantly, large global current account imbalances will not spiral precipitously and a judicious mixture of monetary and fiscal policies will preserve the growth momentum while keeping inflation in check. The region also faces the threat that avian influenza might develop into a pandemic. Other policy challenges facing the region are its fast but inequitable growth and the implementation of the multilateral trade liberalization agenda agreed at the Sixth World Trade Organization Ministerial Conference held in Hong Kong Special Administrative Region of China, in December 2005.

The Asian and Pacific region also needs to address the twin problems of unemployment and underemployment. The incidence of unemployment appears to have increased despite rapid growth in recent years while underemployment remains more serious than unemployment, especially in rural areas. Even within the ranks of the employed the vast majority of workers earn paltry wages and thus remain vulnerable to internal and external shocks. A disturbing aspect of the problem is the

* E/2006/100.

06-32634 (E) 190506

phenomenon of youth unemployment, which appears to be on the rise. Governments thus need to take a number of initiatives to improve the functioning of labour markets, specifically to enhance youth employment, and improve the productivity and earnings of all workers. For their part, employers need to display better corporate responsibility by providing training opportunities for their workers to enable them to enhance their skill levels in today's rapidly changing global economy.

Contents

		Paragraphs	*Page*
I.	Implications of recent economic and social developments	1–27	3
II.	Policy issues and challenges	28–51	10
	A. Oil prices	28–33	10
	B. External payment imbalances	34–38	11
	C. Impact of higher interest rates	39–40	12
	D. Avian influenza	41–43	12
	E. Ongoing challenge of poverty	44–46	13
	F. Remittances	47–48	13
	G. World Trade Organization agenda	49–51	14
III.	Emerging issues of unemployment in the region: rising to the challenges	52–70	15

I. Implications of recent economic and social developments

1. The *Economic and Social Survey of Asia and the Pacific 2006*[1] analyses trends in the regional economy against the background of global developments and outlines the main policy issues facing the region. The 2006 *Survey* also considers unemployment in Asia and the Pacific and examines the actions that Governments can take to deal with the problem.

2. The global economy grew by 3.2 per cent in 2005, down from the record growth rate of 4.0 per cent in 2004. Notwithstanding the slight deceleration, economic performance in 2005 was remarkable in view of an economic environment made increasingly adverse by high and volatile oil prices, widening current account imbalances and a softening of global trade. Growth in 2005 was driven essentially by the strong performance of China and the United States of America.

3. The economic growth rate of developing countries in the Economic and Social Commission for Asia and the Pacific (ESCAP) region decelerated moderately in 2005 (see table). This was the result largely of high oil and commodity prices and the global trade slowdown. More specifically, from an ESCAP perspective, 2004 and 2005 were characterized by a cyclical downturn in the world's information and communication technology (ICT) industry, in which many economies in the region enjoy considerable competitive strength. The rise in oil and other commodity prices, however, increased the level of inflation in 2005 relative to 2004, although the increase in prices throughout the region remained mild by historical standards. Economies overall adjusted well to the higher oil and commodity prices, some attenuating the effects of the latter with continuing subsidization of oil products and others pre-emptively tightening monetary policy in order to dampen inflationary expectations.

4. The current momentum of output growth in the ESCAP region should continue in 2006 while price pressures are likely to abate despite continuing high energy and commodity prices. The following paragraphs provide a brief overview of conditions and prospects for each subregion and groups of countries and outline the main issues confronting them.

5. East and North-East Asia achieved an impressive average economic growth rate of 6.8 per cent in 2005 led by China, which grew by 9.5 per cent in the year as a whole after having achieved double-digit growth in 2004. However, the intention of China to lower demand in "overheated" sectors and the continuing impact of high oil prices could cause the 2006 growth rate for the subregion to dip slightly. The other main economies of the subregion, principally the Republic of Korea and Taiwan Province of China, are leading exporters of ICT and electronic goods. With the global ICT and electronics cycle having bottomed out in the second half of 2005, prospects for increased ICT exports in 2006 are positive and the ICT-exporting economies are expected to grow at a higher rate in 2006 compared with 2005.

[1] *Economic and Social Survey of Asia and the Pacific 2006* (United Nations publication, Sales No. 06.II.F.10.

Rates of economic growth and inflation in selected Asian and Pacific economies, 2003-2006

(Percentage)

	Real GDP				*Inflation*[a]			
	2003	*2004*	*2005*[b]	*2006*[c]	*2003*	*2004*	*2005*[b]	*2006*[c]
Developing economies of the ESCAP region[d]	6.5	7.4	6.6	6.5	4.8	4.7	4.8	4.4
East and North-East Asia	6.5	7.7	6.9	6.5	1.4	3.2	2.2	2.2
China	10.0	10.1	9.6	8.4	1.2	3.9	1.9	2.0
Hong Kong, China	3.2	8.1	7.5	5.4	-2.5	-0.4	1.1	1.6
Mongolia	5.6	10.6	6.0	6.0	4.6	11.0	10.0	6.0
Republic of Korea	3.1	4.6	3.8	4.9	3.6	3.6	2.8	2.9
Taiwan Province of China	3.3	5.7	3.8	4.1	-0.3	1.6	2.3	1.6
North and Central Asia	7.5	7.4	6.9	6.1	12.9	10.2	12.0	9.9
Armenia	13.9	10.1	13.9	7.0	4.8	6.9	0.6	3.0
Azerbaijan	11.2	10.2	26.4	24.8	2.2	6.7	9.6	7.4
Georgia	11.1	6.2	7.7	9.0	4.8	5.7	8.2	3.0
Kazakhstan	9.3	9.6	9.2	8.6	6.4	6.9	7.6	6.7
Kyrgyzstan	6.7	7.1	-0.6	3.0	3.1	4.1	4.3	4.7
Russian Federation	7.3	7.2	6.4	5.7	13.7	10.9	12.7	10.3
Tajikistan	11.0	10.6	6.7	6.8	17.1	6.8	7.8	7.3
Turkmenistan	13.0	9.0	11.0	9.0	6.5	10.0	10.5	11.0
Uzbekistan	4.2	7.7	7.2	7.0	13.1	1.7	7.1	7.4
Pacific island economies	3.0	3.3	2.7	3.0	10.7	3.0	2.2	3.4
Cook Islands	3.1	3.4	3.2	3.0	2.0	0.9	2.9	2.0
Fiji	3.0	4.1	1.7	2.0	4.2	3.3	3.0	3.0
Papua New Guinea	2.9	2.9	3.0	3.5	14.7	2.1	1.0	3.4
Samoa	3.3	3.7	5.6	3.0	0.1	11.7	7.8	3.0
Solomon Islands	5.3	5.0	2.9	2.6	10.0	7.1	6.2	5.0
Tonga	3.1	1.6	2.8	2.8	11.6	11.0	9.6	9.0
Vanuatu	2.4	3.2	2.9	2.2	3.0	1.4	2.5	2.5
South and South-West Asia[e]	7.3	7.4	7.0	7.0	10.4	6.5	7.0	5.7
India	8.5	7.5	8.1	7.9	3.9	3.8	4.5	4.0
Iran (Islamic Republic of)	6.7	4.8	5.0	7.4	15.6	15.2	14.5	11.5
Pakistan	5.1	6.4	8.4	7.0	3.1	4.6	9.3	8.0
Sri Lanka	6.0	5.4	5.5	6.0	6.3	7.6	11.6	6.4
Turkey	5.8	8.9	5.0	5.0	25.3	8.6	7.7	5.8

	Real GDP				*Inflation*[a]			
	2003	*2004*	*2005*[b]	*2006*[c]	*2003*	*2004*	*2005*[b]	*2006*[c]
South-East Asia	5.0	6.4	5.4	5.9	3.1	3.9	5.8	6.0
Indonesia	4.9	5.1	5.6	6.2	6.6	6.1	10.5	11.4
Malaysia	5.4	7.1	5.2	5.9	1.2	1.4	2.9	2.8
Philippines	4.5	6.0	4.8	5.2	3.5	6.0	7.6	7.0
Singapore	1.4	8.4	6.4	6.0	0.5	1.7	0.4	1.2
Thailand	6.9	6.1	4.5	5.7	1.8	2.8	4.5	4.0
Viet Nam	7.3	7.7	8.4	8.0	3.1	7.8	8.4	7.4
Least developed countries	5.6	6.1	5.2	5.8	4.7	5.8	6.3	6.6
Bangladesh	5.3	6.3	5.4	6.0	4.4	5.8	6.5	7.0
Bhutan	6.8	8.7	8.8	8.0	2.1	4.6	5.5	5.0
Cambodia	7.1	7.7	6.3	6.1	0.5	5.6	5.5	3.5
Lao People's Democratic Republic	5.8	6.5	7.2	7.5	15.5	10.5	8.0	7.0
Myanmar	13.8	5.0	4.5	3.5	8.0	—	—	—
Nepal	3.1	3.7	2.6	4.5	4.8	4.0	4.5	5.0
Developed economies of the ESCAP region	1.9	2.4	2.5	2.1	-0.1	0.2	0.0	0.5
Australia	3.3	3.3	2.5	3.2	2.8	2.3	2.8	2.9
Japan	1.8	2.3	2.5	2.0	-0.3	0.0	-0.3	0.3
New Zealand	3.8	4.4	2.2	2.0	1.8	2.3	2.8	3.0

Sources: Economic and Social Commission for Asia and the Pacific, based on national sources; International Monetary Fund, *International Financial Statistics (CD-ROM)* (Washington, D.C., IMF, 2005); Asian Development Bank *Key Indicators of Developing Asian and Pacific Countries 2005* (Manila, 2005 and 2006); Economist Intelligence Unit, *Country Reports* and *Country Forecasts* (London, 2005 and 2006), various issues; and website of the Commonwealth of Independent States Interstate Statistical Committee, http://www.cisstat.com, accessed on 9 January and 10 February 2006.

[a] Changes in the consumer price index.

[b] Estimate.

[c] Forecast/target.

[d] Based on data for 38 developing economies representing more than 95 per cent of the population of the region (including the Central Asian countries); GDP figures at market prices in United States dollars in 2000 (at 1995 prices) have been used as weights to calculate the regional and subregional growth rates.

[e] The estimates and forecasts for countries relate to fiscal years defined as follows: fiscal year 2004/05=2004 for India, the Islamic Republic of Iran and Myanmar and fiscal year 2003/04=2004 for Bangladesh, Nepal and Pakistan.

6. The relaxation by China of its exchange rate regime in 2005 is unlikely to reduce its competitive advantage in exports in view of the limited extent of the currency appreciation so far. However, the large current account surpluses, exceeding in aggregate $190 billion in 2005, are expected to be somewhat smaller in 2006 as a consequence of rising oil prices and the likely appreciation of currencies in the region against the dollar. Although growth in China currently is being driven increasingly by investment and private consumption and less by net exports, overall

growth prospects in the subregion by contrast remain tied to the international trade cycle, particularly ICT exports.

7. In 2005, the countries of North and Central Asia experienced the seventh successive year of growth in gross domestic product (GDP), the longest sustained expansion since the beginning of their transformation to a market-based economic system in 1992. Positive growth was recorded virtually across the subregion in the first eight months of 2005, with Azerbaijan registering remarkable gross domestic product expansion of 20 per cent and Armenia more than 11 per cent. Although high energy and commodity prices are driving such growth rates in the subregion, domestic demand is also playing an important role, with retail turnover growing strongly in Azerbaijan, Kazakhstan, the Russian Federation and Tajikistan in 2005.

8. The strong gross domestic product growth in much of the subregion in 2005 was underpinned by continuing growth in external trade and foreign investment. Owing largely to increased global energy prices, the merchandise exports of Kazakhstan and the Russian Federation to countries not belonging to the Commonwealth of Independent States (CIS) increased significantly in 2005. The trade surplus of the Russian Federation reached $120 billion in 2005 compared with $80 billion in 2004. High energy prices also led to a large increase in the trade surplus of Kazakhstan. However, all other economies in North and Central Asia saw their trade deficits deepen owing to strong growth in the import of intermediate and capital goods, food and raw materials. In Azerbaijan and Georgia the construction of oil and gas pipelines significantly increased imports from both CIS and non-CIS countries.

9. The medium- and long-term prospects for economic growth in the countries of North and Central Asia are based on continuing high energy prices. Should these persist, the Russian Federation is expected to double its gross domestic product by 2010. Kazakhstan plans to boost oil production from 60 million tons in 2004 to between 140 million and 170 million tons by 2015. The countries of North and Central Asia also plan to increase energy and hydrocarbon trade with China, India, Japan, Pakistan and the Republic of Korea; those countries hope to attract additional foreign direct investment to construct and modernize existing energy infrastructure.

10. Lack of reliable data is a major constraint in reporting on the Pacific island countries. However, indications are that, despite continued political instability in that subregion, most Pacific island economies expanded in 2005, owing mainly to the growth of tourism, ongoing diversification in agriculture and the development of the aquaculture and fishing industries. Some countries, such as Papua New Guinea, Solomon Islands and Vanuatu, should also benefit from higher prices for mineral and commodity exports, improved tourism receipts and higher remittances.

11. Political instability in some Pacific island countries affects both domestic and foreign investment as well as economic policy reform initiatives and will inevitably have an adverse impact on future economic growth. Another concern is the falling stocks of certain species of tuna in the subregion, on which several countries depend for revenue. Heavy dependence on increasingly expensive imported oil and diesel fuel is another challenge for these small and vulnerable countries. Some Pacific island countries have improved their fiscal position in recent years, which has contributed to the easing of inflation. However, the high oil prices are expected to exert pressure on overall prices in these countries and are prompting renewed

regional interest in alternative fuel sources, such as ethanol made from local sugar cane.

12. Despite rising oil prices, countries in South Asia maintained their growth momentum in 2005. Aided by normal monsoon rains, the reforms and structural changes initiated earlier are now bearing fruit. The increasing integration of the subregion into the global economy, rising consumer spending and generally supportive policies are also helping the pace of growth. Both India and Pakistan have achieved impressive growth rates in recent years. On the basis of sustained high economic growth, India is increasingly becoming a major contributor to global growth. In addition to an almost normal harvest in 2005, the strong responsiveness of the private sector to emerging opportunities has sustained robust growth in both industry and services. The capital and consumer goods sectors are performing well, indicating an improvement in consumer and investment demand. The economy of India is also benefiting from substantial inflows of foreign investment. That Government's efforts to contain the fiscal deficit despite higher public expenditures for an employment-generation programme have served to minimize the crowding out effects of Government spending on private investment. Notwithstanding the strength of domestic demand, the external sector remains a major source of strength for the economy.

13. The economy of Pakistan grew strongly in 2005 at the highest rate in the past two decades. This impressive growth rate was supported by strong growth in large-scale manufacturing, especially in textiles, a sharp upturn in agriculture and a robust performance in the service sector, especially finance. Moreover, strong growth was underpinned by supportive macroeconomic policies, growth in domestic demand, renewed confidence of the private sector, greater fiscal discipline and a stable exchange rate.

14. Both India and Pakistan are projected to maintain their current growth momentum in 2006 and beyond. All three main sectors, namely, agriculture, industry and services, are expected to contribute to the healthy growth of the two economies. It is worth noting that in October 2005 Pakistan suffered a devastating earthquake in the northern areas of the country that resulted in a major loss of life and property. The country's long-term reconstruction needs are likely to be massive, approximately $5.2 billion. There are indications, however, that the economy as a whole is not likely to lose momentum in the short term as a result of the earthquake.

15. In Sri Lanka, recent growth momentum was maintained in 2005. Growth in the agricultural and industrial sectors improved owing to favourable weather conditions supported by improvements in both export and domestic markets. The initial relief work following the December 2004 tsunami tragedy has been surpassed by longer-term reconstruction and rehabilitation efforts. Expenditures on such work could be reinforced owing to the improved earnings generated in other sectors of the economy. Consequently, a higher growth rate is projected for 2006.

16. High energy prices continue to underpin the performance of the Islamic Republic of Iran. Nevertheless, the non-oil economy and agriculture are also making significant contributions, with the private sector becoming more active in the economy. The economy of Turkey slowed sharply in 2005 primarily in response to higher energy prices, which created significant uncertainty for both investors and households. Current trends are likely to continue in both countries in 2006.

17. Across the subregion, macroeconomic stability is being maintained through budgetary discipline and prudent monetary policy, although price pressures have re-emerged in Turkey. However, the increase in inflation in Pakistan and Sri Lanka was substantial (over 4 percentage points) in 2005 compared with that of 2004. Higher oil prices and increased imports have deepened the current account deficits in the subregion. With comfortable reserves, exchange rates have remained stable but prudent macroeconomic management will be needed to prevent the deficits from becoming a problem.

18. Over the next 12 months containment of inflationary pressures amid rising oil prices has to be the principal priority. A judicious combination of fiscal and monetary policies can help in limiting increases in consumer prices. Some countries in the subregion experiencing rapid output growth are also witnessing a credit boom. It is important to remain vigilant as the containment of credit booms requires strengthened surveillance of the banking system and close scrutiny of corporate and personal borrowing if the problem of non-performing loans is to be avoided in the future.

19. In the subregion as a whole, renewed focus is being placed on the development of physical infrastructure in order to overcome past deficiencies and to accelerate future growth. Most countries have realized that they do not have adequate physical infrastructure for enhanced private investment and sustainable rapid economic growth. For example, rapid output expansion is not being matched by expansion in transport, ports, energy and water, and this contributes to a rising gap between supply and demand. From a subregional perspective considerable potential exists for mutually beneficial trade in energy and water resources to develop new, and to improve existing, transport corridors and to bolster the efficiency of transport and trade facilitation services.

20. Economic growth in the South-East Asian subregion eased in 2005 after unusually good performance in 2004, when strong global demand for manufactures, especially electronics and ICT products, had driven growth. Despite the doubling of oil prices between 2002 and 2004 and their continued rise in 2005, the region did not experience any marked increase in price pressures until the second quarter of 2005. The extensive use of oil subsidies muted the pass-through effects of higher oil prices on the cost of final goods. However, this resulted in a heavy fiscal burden which made the continuation of subsidies unsustainable from the middle of 2005. Many countries have therefore been phasing out oil subsidies and, as a consequence, inflation is likely to creep up in 2006. In general, the policy responses of individual countries to oil subsidies can be expected to influence the extent of inflation.

21. Economic growth in the subregion is expected to accelerate in 2006, as the cyclical recovery of demand for semiconductors and ICT products gathers pace and is aided by continuing growth in Japan and the United States. Within the subregion, increased imports are forecast by Malaysia and Viet Nam, the region's net oil exporters, which will benefit from high oil prices.

22. Monetary policy was tightened in response to the increasing inflationary pressures occurring after the second quarter of 2005; this firmer stance is expected to continue into 2006. Assuming that oil prices do not rise much above their 2005 levels, overall inflation in the subregion should decline marginally in 2006. Higher interest rates, aided by a degree of appreciation of the exchange rates for some currencies in the subregion, are expected to partially offset the higher prices of

dollar-denominated oil and other imports. Fiscal policy in the region is expected to be generally neutral, although Thailand is expected to continue applying a moderate amount of fiscal stimulus in 2006.

23. Economic growth in Japan accelerated in 2005. Japan is witnessing a recovery in private consumption, which is buttressing higher investment expenditures by corporations. This has been essentially a consequence of the structural reforms implemented in the banking and corporate sectors, which also improved profitability in both sectors. However, the problem of deflation continues to affect consumer sentiment in Japan while the overall tenor of macroeconomic policies is bedevilled by the country's huge public debt. Looser monetary policies are expected to help to end deflation in 2006. However, fiscal consolidation appears to be some way off and is likely to generate uncertainties vis-à-vis the real strength of domestic demand and the impact of higher interest rates on the overall fiscal outcome.

24. In the other two developed countries of the region, Australia and New Zealand, gross domestic product growth eased in 2005 compared with 2004 but remained close to its long-term trend, as strong export growth was partly offset by weaker domestic demand. A sharper decline in domestic demand and still buoyant imports in 2006 are likely to slow the New Zealand economy further. By contrast, the continued strength in exports and high commodity prices, along with subdued import demand, are likely to bring the economy of Australia back to its recent growth trend of over 3 per cent in 2006. The fiscal position of both countries remains strong owing to their relatively buoyant tax revenues. In Australia, a fiscal surplus was achieved despite substantial tax cuts. Both countries remain cautious about a build-up of inflationary pressures resulting from the rise in energy and overall producer prices and emerging capacity constraints. Interest rates have remained stable: the last rise in Australia was in March 2005 and in New Zealand, in October 2005. Moreover, consumer price inflation remains within the target ranges of the central banks of those countries.

25. Both Australia and New Zealand continue to face the problem of a sizeable current account deficit: nearly 5 per cent of gross domestic product in Australia and over 7.5 per cent in New Zealand. Financing this gap is not a significant policy issue per se, but it does serve to circumscribe both countries' freedom to manoeuvre with regard to monetary policy because it creates a floor below which interest rates cannot fall. While a number of temporary influences are at work in increasing or decreasing the current account deficit, such as repatriation of investment income by foreigners and fluctuations in commodity prices and tourist arrivals, it is the lack of domestic savings that is the fundamental cause of the current account imbalance in both countries.

26. Among the least developed countries in the region, the economy of Bangladesh has been experiencing steady growth in recent years. A slight acceleration in growth is expected in 2006, aided in part by flood-related reconstruction work and bumper crops. Steady gross domestic product growth in Bangladesh has been translated into visible progress on the social front and is reflected in the country's upgrading to the category of a medium-developed country in the United Nations Development Programme human development index. In Nepal, gross domestic product growth decelerated in 2005 owing to poor performance in both the agricultural and non-agricultural sectors. Inclement weather was primarily responsible for the slower growth in agriculture and the country's

internal conflict caused a slowdown in the broader economy. If the improved weather conditions remain steady, growth in 2006 is expected to revert to its recent trend. In Cambodia, the Lao People's Democratic Republic and Myanmar, the pace of gross domestic product growth was broadly maintained in 2005 but price pressures increased. Prospects for 2006 indicate a continuation of these trends accompanied by an easing of inflation.

27. Despite recent progress, poverty remains pervasive in most of the least developed countries in the region. Therefore, Governments need to give priority to promoting rapid and sustained economic growth. The primary goal must be to double average household living standards as quickly as possible, since the average level of private consumption per capita is so low. More than a simple expansion of gross domestic product is required. Economic growth must be based on the accumulation of capital, skills and productivity growth and the expansion of sustainable livelihoods and employment opportunities that would expand the consumption possibilities of households and individuals. While economic growth is of paramount importance for poverty reduction in the least developed countries, inequality and exclusion cannot be ignored. Efficiency-expanding redistribution of assets and income are important for sustained economic growth and poverty reduction in situations of generalized poverty.

II. Policy issues and challenges

A. Oil prices

28. Oil prices have doubled since the beginning of 2004 and have trebled since 2002. Despite the high oil prices there has been no sign yet of a global economic slowdown for three major reasons. First, the increase in oil prices has been driven mainly by strong global demand, not supply disruptions as had occurred in the past. The adverse effect on growth is far lower in a demand-driven price rise than one which is caused by a disruption in supply. Second, both inflation and inflationary expectations are lower worldwide, compared with expectations at the time of the previous oil shocks. Finally, the intensity of oil consumption and production, particularly in the middle-income developing countries, is significantly lower than in the 1980s.

29. Notwithstanding these matters, because Asia and the Pacific is highly dependent on oil, the region remains vulnerable to any significant increase in oil prices in 2006. Net oil-importing countries need to take steps to adjust to this risk, both to mitigate the adverse social impacts of high oil prices and to counter their negative macroeconomic effects. For 2006 the *Survey* has assumed that oil prices will continue to fluctuate within the range of $50-$55. There are fears, however, that oil prices could trend upwards towards $100 a barrel within the next four years.

30. A streamlining of the existing system of subsidies is clearly warranted, particularly when they do not protect the intended groups. Governments could start by phasing out subsidies on fuel types that are not widely used by the poor. For example, diesel subsidies, though widespread in the region, do not directly benefit the poor as do, for instance, subsidies on liquefied petroleum gas or kerosene. A better approach would be to replace oil subsidies with direct income-targeting instruments that would benefit the poor.

31. Least developed countries in particular face significant vulnerabilities as a result of rising oil prices. These countries have little access to alternative sources of financing to cushion them against a temporary increase in their balance of payments deficit caused by high oil prices. Thus, international financial institutions need to provide, or arrange, financial assistance for the least developed countries, as was done in the 1970s through the International Monetary Fund oil facility.

32. Net oil exporters in the region, for example those in Central Asia, also need to adjust to rising oil prices. The focus should be on how to manage oil windfalls efficiently without jeopardizing short-term macroeconomic stability, as there is likely to be pressure on the real exchange rate to appreciate.

33. Both oil-importing and oil-exporting countries need to develop a longer-term policy response to reduce oil dependency, to improve energy efficiency and to promote energy conservation. Rationalization of energy pricing, greater public awareness of alternative energy options, improved regulations to ensure a minimum level of energy efficiency and fiscal incentives to reduce energy consumption are some of the measures that have proven to be effective in various settings. Their wider application should be promoted as a matter of priority in the region.

B. External payment imbalances

34. The widening imbalances in the external accounts of major economies in the world pose a major economic risk for the ESCAP region in 2006. A precipitous spiralling of these imbalances could create large upheavals in the international financial markets and cause significant exchange rate instability not involving the dollar alone but perhaps several currencies in the region as well. Such phenomena would, in turn, have a negative impact on the regional economy by making both consumers and investors more risk averse and more likely to divert savings into real estate and precious metals even more than is currently the case.

35. There is only limited scope for action to address this problem at the national level. At the regional or international level, one approach would be to focus on the current account balances per se. Since one country's deficit is another's surplus, one policy response could be to cause the currencies to appreciate in surplus countries while they depreciate in deficit countries. As a result, deficit countries would improve their export competitiveness and thus improve their current account balances. The opposite would be true for surplus countries. However, such a response may not prove effective in view of the fact that the price elasticities of internationally traded goods tend to be limited in the short term and consumer choice is not a matter of price alone. Moreover, exchange rate changes are not simply matters of administrative fiat.

36. A more appropriate policy approach would be to regard current account imbalances as a reflection of structural imbalances between domestic savings and investment. Those countries with excess savings compared to investments tend to run current account surpluses. The opposite is true for countries with low savings. Remedying the imbalances therefore requires higher investments in the surplus countries and higher savings in deficit countries, the United States in particular; however, significantly raising the levels of savings and investments cannot be done over the short term.

37. Given the widespread negative implications of an abrupt and large-scale spiralling of global current account imbalances if left to the financial markets alone, there is a need, too, for a concerted regional response, if not a global one. Rather than trying to correct imbalances that may lead to sharp contractions in the wider regional or global economy, a more effective solution would be one that strives for a balanced, medium-term approach, with exchange rate adjustments effected over a period of time within an agreed regional framework.

38. Within such a framework countries in the region with current account surpluses would need to significantly bolster investment in their economies. There is obvious scope for increased investment in the region, particularly in view of the enormous need for new investment in infrastructure, both physical and social.

C. Impact of higher interest rates

39. An important issue with which economies in the region would have to deal in 2006 is the potentially adverse impact on growth of a combination of tighter fiscal and monetary policies. For a number of years, many countries have been following a policy of fiscal consolidation with a view to reducing the growing burden of public debt and providing more space for private investment activity. Inflationary pressures induced by high oil prices have resulted in a tightening of monetary policy and rising interest rates across the region, although there are some notable exceptions. Reinforcing the effects of long-term fiscal consolidation, especially in countries where it is being brought about through cuts in Government expenditure rather than through improved tax revenues, higher interest rates are bound to affect the pace of economic activity. In fact, a particular danger exists in those countries where low interest rates have fuelled strong growth in debt-financed private consumption and created asset bubbles.

40. In this regard, higher interest rates should prove less deleterious for economic growth than cuts in Government spending, especially in the poorer developing countries where Government development expenditure is often the key to the pace of development. However, in the richer developing countries where real interest rates are already high, a further significant increase could result in a hard landing for the economy through a sharp drop in asset prices. The policy challenge therefore is to judiciously mix fiscal and monetary policies in order to ensure steady output growth over the next 12-18 months. Most investors value policy predictability; Governments should therefore develop medium-term scenarios for gross domestic product growth, inflation, budgetary and balance-of-payments outcomes through a process of consultation with all relevant stakeholders.

D. Avian influenza

41. Avian influenza is a viral infection primarily affecting birds but sometimes also mammals, including humans. Until recently, the current outbreak of avian influenza had affected mainly poultry in East and South-East Asia. Between December 2003 and February 2006, there were 161 human cases in the region with 86 deaths. No vaccine is currently available to protect humans from avian influenza.

42. The estimates of deaths from a possible global pandemic of highly pathogenic avian influenza range from 5 million to 150 million people. As a conservative

estimate, the global loss in gross domestic product from a pandemic could amount to $200 billion in just one quarter and in a worst-case scenario could plunge the global economy into recession. The costs of dealing with the wider spread of the disease have so far been around 0.1 per cent of gross domestic product. However, should it emerge in the form of a pandemic involving rapid human-to-human infection, the influenza would inevitably cause massive disruption to everyday life through widespread quarantines and travel restrictions and impose a huge burden on public-health budgets.

43. Given these risks, there is an urgent need for collective preparedness in the region involving the stockpiling of medical supplies and taking joint action on possible control measures, such as travel restrictions, to minimize the spread of the disease. It is also important from the standpoint of cost-effectiveness to concentrate resources and action on controlling the disease at the source before it develops into a more rapidly spreading contagion.

E. Ongoing challenge of poverty

44. Although the Asian and Pacific region has been growing faster economically than most parts of the world for two decades or more, the eradication of poverty remains its most important challenge. In tackling the problem of poverty it is important to remember that rapid economic growth remains the surest route for reducing both income poverty and non-income poverty. Rapid economic growth provides opportunities for employment in both the formal and informal sectors of an economy and it generates resources for the public sector. In this manner, issues of non-income poverty, such as insufficient or poor-quality public goods, namely education, health, transport and housing, can be meaningfully addressed.

45. However, rapid growth alone may not be enough. It appears that in countries where poverty is widespread, jobs and income growth alone will not have a positive impact on non-income poverty. In such cases, the Governments concerned need to intervene to make the growth process more equitable by expanding the provision of and access to public goods, particularly for and by the poor.

46. Inequitable growth is an important issue in many smaller economies, including least developed countries and Pacific island States. In such economies, national efforts can be severely undermined by the paucity of financial and non-financial resources and further eroded by physical remoteness, as in the case of the Pacific island countries. In such countries, without regional and, indeed, international aid and support, such as the global compact envisioned in the eighth Millennium Development Goal, the prospects for sustained long-term growth and, hence, for reducing poverty, are very limited. In that broad context, the temporary movement of workers on contract employment abroad is an option with considerable potential for reducing poverty.

F. Remittances

47. Remittances sent by migrants and temporary workers on contract abroad to their families have greatly helped to raise the standard of living of some of the poorest sections of society in South Asia, South-East Asia and the Pacific region. Countries with high levels of underemployment and with limited opportunities for

formal sector employment could follow the example set by the Philippines and systematically promote the temporary export of workers as part of a national development and poverty-reducing strategy.

48. Equally, countries facing general labour shortages or shortages of people with specific skills should actively consider allowing migrant workers to work legally in their economies without fear of harassment.

G. World Trade Organization agenda

49. The Sixth World Trade Organization Ministerial Conference, held in Hong Kong Special Administrative Region of China, in December 2005, concluded with the adoption of a wide-ranging Ministerial Declaration. New elements in the Declaration include the following:

- An end to all agricultural export subsidies by the end of 2013, with progressive phasing-out such that a substantial number of subsidies would be phased out by the end of the first half of the implementation period, as well as an end to all export subsidies for cotton by developed countries in 2006.
- For non-agricultural market access, higher tariffs will be reduced more steeply than lower tariffs, thus leading to a more harmonized (flatter) tariff structure across all World Trade Organization members.
- Duty-free and quota-free access "on a lasting basis" by developed and developing countries declaring themselves in a position to do so, for at least 97 per cent of exports (as defined at the tariff line level) from the 32 least developed countries that are World Trade Organization members, by 2008 or no later than the start of the implementation period. However, the products most likely to fall into the 3 per cent category are those very products in which least developed countries are the most competitive and for which they would stand to gain the most from unfettered access to developed markets: textiles and clothing products from the least developed countries in Asia and the Pacific would feature prominently in this category. Notwithstanding these concerns, this measure represents a step forward on an issue that has been on the agenda for more than a decade.
- Intensification of the request-offer negotiations in services, which remain the main method of negotiation, with a view to securing substantial commitments. A second round of revised offers is to be submitted by 31 July 2006, while a draft schedule of commitments in services is scheduled for completion by 31 October 2006.

50. While the Declaration puts the Doha round back on track, an issue of fundamental importance is whether it holds the promise that the Doha round will ultimately correct the development deficit of the Uruguay round. A key challenge facing ESCAP members and associate members over 2006 will be how to reinvigorate the Doha development agenda.

51. Developing economies in the ESCAP region are likely to be challenged in the months ahead to make concessions of a commercial value so that developed countries will remain committed to the process. Thus, the challenge facing the trade-dependent economies of the region is how they might harness the traditional

reciprocity dynamics of the World Trade Organization to move forward on their market access expectations. At the same time, a jump-start from the region is needed to open up the service sector, and efforts made in this regard by one or two increasingly dynamic service exporters from this region would be worthy of further support by other developing economies of the region.

III. Emerging issues of unemployment in the region: rising to the challenges

52. The number of people unemployed in East Asia increased from 4 million in 1992 to 9 million in 2002, while in South-East Asia and the Pacific the number increased from 5.5 million to 14.6 million. Total unemployment increased by 7 million in South Asia over the same period. The rate of unemployment increased from 2.5 per cent in 1994 to 3.6 per cent in 2004 in East Asia and from 4.1 per cent to 6.4 per cent in South-East Asia. South Asia experienced an increase in the unemployment rate from 4.0 per cent to 4.8 per cent during the same period. The phenomenon of underemployment, particularly in rural areas, is even more widespread than unemployment itself. Sadly, the region also harbours an estimated 127 million, or 52 per cent, of the world's 246 million working children between the ages of 5 and 14.

53. Over the years, the economic structure of the region has moved towards employment in manufacturing and services and away from agriculture. However, the share of employment in the agricultural sector vis-à-vis total employment, particularly in large economies, remains high. In many countries the rural informal economy still provides the majority of employment opportunities; however, such employment tends to prefer male workers. The changing structure of the regional economy has also resulted in a widening wage gap between skilled and unskilled workers.

54. There are two main reasons for the high rates of unemployment and underemployment. First, the labour-force growth rate is high. It grew by 2.4 per cent per year in South-East Asia and the Pacific and by 2.2 per cent in South Asia during the past decade, owing to several factors: high birth rates, increasing female participation rates and extended working ages. Second, the pace of job creation has not kept up with the growth in the labour force. In addition, there has been lower demand for labour as a result of technological change and the considerable downsizing that has occurred in public-sector employment following privatization.

55. There is now widespread concern that many countries in the region are achieving high output growth at the expense of employment creation. Jobless growth is occurring, particularly in rapidly growing economies where the rate of unemployment has tended recently to rise.

56. A large share of those employed in the region earn paltry wages. The share of the working poor measured in terms of employees earning less than $2 a day (defined in terms of purchasing power parity) as a share of total employment was as high as 88 per cent in South Asia in 2003, 59 per cent in South-East Asia and 49 per cent in East Asia. These figures indicate that the vast majority of the people employed in these subregions earn wages that are just above the $1 a day poverty

line. As a result, the likelihood is very high that the working poor could fall prey to internal or external shocks and slide into extreme poverty.

57. Unemployment in the region is highly concentrated among youth. For example, while the overall unemployment rate in the region was about 4.4 per cent in 2004, the rate of youth unemployment varied between 7.5 per cent in East Asia and 17.1 per cent in South-East Asia. The rate more than doubled in South-East Asia, from just under 5 million in 1994 to nearly 10.5 million in 2004. South Asia has the largest number of unemployed youth, at almost 14.5 million in 2004.

58. Improving the functioning of labour markets is of vital importance in order to tackle the problem of unemployment. In the formal sector, the region's labour markets are excessively rigid owing to the non-transferability of pension benefits, firm-specific training and strict firing regulations. The introduction of more flexible contributory pension and retirement schemes, minimum standards of education and technical skills and a relaxation of hiring and firing regulations along with better income protection for laid-off workers at the societal level could help to address these issues.

59. The low level of education and the mismatch between educational attainment and the skills demanded by the private sector are major causes of unemployment. Workers with more than a minimum level of education appear to perform better in on-the-job training, skills testing and evaluation, thus increasing their employability and job prospects.

60. Compulsory education up to a fixed age could help to address the complex issue of child labour. Where female unemployment is high or the female participation rate is low, educational reforms may help to break this vicious circle by providing a more conducive sociocultural environment for women to receive an education, to improve their productivity and to help in eliminating wage and employment discrimination against women.

61. Vocational training programmes in many developing countries of the region do not seem to receive strong technical and practical support despite the potential high returns of such programmes. There are many reasons for this, such as trainers lacking recent industrial exposure and educators lacking professionalism in curriculum development. Training programmes are most effective when they are tightly targeted and small-scale, with a strong on-the-job component and linked to industry.

62. Interventions to enhance the employability of youth should be a key component of active labour-market policies and educational reforms. Programmes facilitating labour-market entry need to target youth well in advance of their entry into the formal labour market. Career guidance and counselling and the provision of labour-market information would be useful tools in steering youth in the right direction.

63. Credible reform of public-sector recruitment and wage policies could also control high unemployment by reducing the incentives for extended job searches. Reform of such policies to eliminate the bias associated with public sector jobs perceived as "good" and create conditions for improvement in the quality of "bad" jobs would be necessary to solve the problem of people searching for public sector jobs over an extended period.

64. Although unemployment benefit schemes have major fiscal implications, they could serve as a safety net for workers during short spells of unemployment and help to make labour markets more flexible. To be more effective, unemployment benefits should be linked to the development of job skills during the period of unemployment.

65. The success of some countries such as Malaysia in stimulating employment growth through trade liberalization provides evidence of the importance of a balanced approach to economic growth and employment generation. An initial step in obtaining benefits from trade liberalization would be to improve absorptive capacity in the host country, particularly by enhancing the quality of human resources. Providing a supportive environment, both in terms of domestic reforms and enabling greater access to global markets, is also required for a country to benefit from trade liberalization.

66. To strike the right balance between high economic growth and employment creation requires steps to improve the productivity of workers in niche industries while focusing on sectors where the majority of labour is concentrated and giving particular emphasis to capacity-building. In agriculture, a number of measures would play a critical role in this respect: land reform, extension services, provision of credit, crop diversification and rural infrastructure development. Improved marketing facilities and cooperative organizations could also be effective instruments for advancing rural employment.

67. The development of microenterprises and small and medium-sized enterprises in both rural and urban areas possibly offers the greatest potential for employment generation. Therefore, this process needs to be facilitated through the provision of a conducive business environment, in particular by reducing entry costs, providing infrastructure, building capacity and good governance. The private sector in many developing countries in the region is hampered in the development of an environment conducive to business by inconsistent policies and weak implementation of relevant laws, frequent legal changes, the considerable discretionary powers of local authorities and bureaucratic harassment, complicated and lengthy procedures to register firms, stringent licensing and permit regimes and high taxation. Overcoming these constraints is essential for providing an enabling business environment in which microenterprises and small and medium-sized enterprises can develop.

68. Employers also need to display better corporate responsibility by providing opportunities for the training and retraining of workers, by collaborating with the public sector in providing opportunities for unemployed youth to obtain training and by ensuring workplace safety and the welfare of employees. Social dialogue is a key instrument for maintaining good industrial relations.

69. International migration could play a valuable role in stabilizing the labour markets of both labour-importing and labour-exporting countries. In this respect, a rule-based flow of persons under a global framework, such as mode 4 of the World Trade Organization General Agreement on Trade in Services, could help all countries to achieve tangible benefits.

70. The Commission is invited to direct the Secretariat to consider further any of the above-mentioned matters.